UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

JAN 10 1984

Honorable John D. Dingell
Chairman, Committee on Energy
and Commerce
U.S. House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

The Department of Commerce has reviewed H.R. 1415, a bill

> "To protect franchised automobile dealers from unfair price discrimination in the sale by the manufacturer or importer of new motor vehicles,"

and we hereby submit our views on the legislation.

Under H.R. 1415, an automobile manufacturer would be prohibited from (a) selling or leasing any passenger car, truck or station wagon to any person at a price lower than that accorded to its franchised dealers; (b) imposing upon a dealer any restrictions that are not imposed upon all other purchasers; and (c) providing to a purchaser any rebate or discount that is not provided to all purchasers. In addition, a manufacturer would be unable to sell a vehicle to any person for resale to a unit of federal, state or local government at a price which is lower than the price at which the vehicle is sold to a dealer during the same period for resale to a unit of government.

We oppose enactment of H.R. 1415. Despite its avowed intention to provide protection against "unfair price discrimination," in reality the bill would prohibit marketing practices that vehicle manufacturers and their fleet customers have found highly efficient and mutually beneficial. We believe H.R. 1415 is anti-competitive and designed to benefit the special interests of franchised automobile dealers at the expense of American consumers.

H.R. 1415 would eliminate competition in the fleet sales market by prohibiting large volume fleet purchasers, including the federal government, from negotiating with automobile manufacturers for lower prices. We believe that large volume fleet purchasers,

Prepared by: OAGC/L Lisa Lindeman 377-1328

bcc: EA (C. Miller)
IPM Chron
GC Chron
File H.R. 1415
Lisa Lindeman

including the federal government, should be allowed to negotiate with manufacturers for lower prices in order to enhance competition and encourage efficient allocation of resources.

We understand that the Department of Justice is opposed to the bill because it would prohibit discounts on direct sales by manufacturers both to governmental and commercial fleet purchasers, and that the Department intends to submit a report outlining its opposition to the bill which will focus on its undesirable effects.

We have been advised by the Office of Management and Budget that there is no objection to the submission of this letter to the Congress from the standpoint of the Administration's position.

Sincerely,

Irving P. Margulies

Irving P. Margulies
Acting General Counsel

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

JAN 10 1984

Honorable Peter W. Rodino
Chairman, Committee on the Judiciary
U.S. House of Representatives
Washington, D.C. 20515

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Sincerely,

Irving P. Margulies

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Acting General Counsel

THE WHITE HOUSE

WASHINGTON

June 6, 1984

MEMORANDUM FOR BRANDEN BLUM
LEGISLATIVE ATTORNEY
OFFICE OF MANAGEMENT AND BUDGET

FROM: JOHN G. ROBERTS
ASSOCIATE COUNSEL TO THE PRESIDENT

SUBJECT: DOJ Draft Testimony on H.R. 5305 and H.R. 1415, Bills to Protect Franchised Automobile Dealers and Consumers From Unfair Price Discrimination in Sale by Manufacturers of New Vehicles

Counsel's Office has reviewed the above-referenced draft testimony, and finds no objection to it from a legal perspective.

ID # _____ CU

WHITE HOUSE
CORRESPONDENCE TRACKING WORKSHEET

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Name of Correspondent: James Muir

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Subject: DOS draft testimony on H.R. 5305 and H.R. 1415, bills to protect franchised automobile dealers and consumers from unfair price discrimination in sale by manufacturers of new vehicles

ROUTE TO:		ACTION		DISPOSITION		
Office/Agency	(Staff Name)	Action Code	Tracking Date YY/MM/DD	Type of Response	Code	Completion Date YY/MM/DD
CUTOLL		ORIGINATOR	84/06/05			1 1
		Referral Note:				
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D - Draft Response
F - Furnish Fact Sheet to be used as Enclosure
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EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

SPECIAL

June 5, 1984

LEGISLATIVE REFERRAL MEMORANDUM

TO: LEGISLATIVE LIAISON OFFICER

Department of Commerce (LRM only)
Department of Defense - Werner Windus - 697- 1305
Federal Trade Commission (LRM only)
Department of Transportation - John Collins - 426-4694
General Services Administration - Ted Ebert - 566-1250

SUBJECT: DOJ draft testimony on H.R. 5305 and H.R. 1415, bills to protect franchised automobile dealers and consumers from unfair price discrimination in sale by manufacturers of new vehicles

The Office of Management and Budget requests the views of your agency on the above subject before advising on its relationship to the program of the President, in accordance with OMB Circular A-19.

Please provide us with your views no later than 10:00 A.M. Wednesday, June 6, 1984. (NOTE: A hearing is scheduled for Thursday June 7. Also agency reports opposing H.R. 1415 have been previously circulated for review and cleared.)
Direct your questions to Branden Blum (395-3802), the legislative attorney in this office.

James C. Murr for
Assistant Director for
Legislative Reference

Enclosure

cc: K. Wilson, J. Cooney, J. Dyer, K. Schwartz, R. Howard, L. Li, M. Uhlmann, F. Fielding

DRAFT

STATEMENT

OF

CHARLES F. RULE
DEPUTY ASSISTANT ATTORNEY GENERAL
ANTITRUST DIVISION

BEFORE

THE

COMMITTEE ON ENERGY AND COMMERCE
SUBCOMMITTEE ON COMMERCE, TRANSPORTATION AND TOURISM
HOUSE OF REPRESENTATIVES

CONCERNING

AUTO MANUFACTURER'S PRICING POLICY - H.R. 5305

ON

JUNE 7, 1984

Mr. Chairman and Members of the Committee: I am pleased to have the opportunity to provide you with the views of the Department of Justice on H.R. 1415 and H.R. 5305, bills "to protect consumers and franchised automobile dealers from unfair price discrimination in the sale by the manufacturer of new motor vehicles." For the reasons I will discuss, the Department of Justice strongly recommends against enactment of this legislation.

I. Description of the Bills and the Existing Motor Vehicle Distributional System

While these bills are similar in that their essential feature is to prohibit price differentials to different classes of motor vehicle purchasers, they are different in certain respects. H.R. 1415 would substantially expand the "Automobile Dealers' Day in Court Act," 15 U.S.C. 1221 et seq., which governs certain relations between automobile manufacturers and their dealers. Section 1 (a) of H.R. 1415 provides that each franchise agreement between a motor vehicle dealer and manufacturer shall be deemed to prohibit the manufacturer from: (1) selling or offering to sell any vehicle to any person (including any other dealer) during any period of time at a price lower than that charged to its franchised dealers for the same, similarly equipped model during the same period of time; (2) imposing or enforcing any restriction on its dealers not imposed or enforced against any other purchaser; and (3) providing ultimate purchasers with any rebate,

discount, refund, promotional service, additional equipment, or any other inducement or benefit not provided to all other ultimate purchasers of the same model during the same time period. An exception to prohibition (1) above permits the manufacturer to sell a vehicle to any person (including any other dealer) for resale to any unit of federal, state, or local government, but only if the manufacturer does not sell or offer to sell the same, similarly equipped model to any other person for resale to any unit of government at any period of time at a price lower than that charged to the franchised dealer.

H.R. 5305, on the other hand, takes a somewhat different approach to achieve essentially the same result. Section 2 of that bill provides that no motor vehicle manufacturer may sell or lease any new vehicle to any person (including a dealer) during any sales period at a price higher than the lowest price at which any other vehicle of the same model, similarly equipped, is sold or leased, or offered for sale or lease, by the manufacturer during that sales period. Section 3 provides an exception allowing the manufacturer to sell or lease, or offer to sell or lease, any new vehicle to (1) a non-dealer employee of the manufacturer; (2) any department, agency, or instrumentality of the United States or of a State or local government; (3) or the American Red Cross. A further exemption in Section 3 permits the sale or offer to sell any new vehicle to any purchaser, if such sale or offer to sell by the

manufacturer is part of a qualified regional incentive sales program for a designated region. To so qualify, all vehicles of the same model, similarly equipped, sold or offered for sale by the manufacturer in the region during the period, must be sold and offered at the same price, and all vehicles sold in such region during such period must be delivered by the manufacturer to the purchaser in such regions.

Both bills would permit persons to bring actions against motor vehicle manufacturers for damages and injunctive relief based upon violations of the prohibitions contained in the respective bills. In addition, H.R. 5305 permits awards of punitive damages and attorneys fees in the discretion of the court.

Both bills would substantially alter motor vehicle manufacturers' existing relationships with their dealers and the present distribution system for such vehicles. As such, they appear to be based upon some belief that the existing distribution system for motor vehicles is not efficient and is flawed in ways that ultimately harm consumers. However, it is in the manufacturers' interest to choose the most efficient distribution system possible, so as to minimize the costs of distributing motor vehicles to ultimate consumers and thereby maximize their profits. We are aware of no evidence that the existing distributional system is inefficient, nor are we aware of any reasons why manufacturers would choose an inefficient distribution system.

Currently, manufacturers distribute the great majority of their motor vehicles to franchised dealers, who provide particular services as desired by individual consumers and other low-volume purchasers. Manufacturers also distribute some of their vehicles directly to high-volume purchasers, such as governmental units, taxi fleet operators, and rental car companies, who use those vehicles to provide products or services to consumers. Information we have seen indicates that, at present, high-volume sales account for only approximately 20% of the current motor vehicle market. The remaining 80% of such sales are made through franchised dealers.

Different groups of vehicle users value particular distribution services differently and are, therefore, willing to pay different amounts for those services. Thus, for example, an individual who desires to purchase an automobile for personal (or even business) use from a franchised dealer will demand a certain mix of services. Some of those services will be provided by the manufacturer (e.g., installation of certain options, warranty terms, and delivery to the dealer), while other services will be provided by the dealer (e.g., sales efforts, demonstrators, road preparation, and repair work under the warranty).

High-volume purchasers, on the other hand, may be willing to forego certain services or perform them themselves, saving manufacturers those costs and enabling them to charge such

purchasers less than the price charged to franchised dealers. In addition, there may be some benefits to manufacturers as a result of use of their vehicles by high-volume purchasers that also benefit franchised dealers. For example, consumers get valuable information about the operation of vehicles they rent that may factor in their purchase decisions, and rental car company advertisements about the cars they lease likewise benefit both the manufacturers of those cars and their franchised dealers. The imporant point, however, is that through whatever channel the vehicles are distributed, consumers ultimately must bear the costs of the distribution system as purchasers of vehicles, as ultimate users of transportation services, and as taxpayers.

The ability of manufacturers to adjust their charges according to different services provided enables them to satisfy the varying demands of their different classes of purchasers at prices that reflect the costs of the services provided. If, as we believe, the existing system is efficient, then enactment of H.R. 1415 or H.R. 5305 may require some customers to pay for services they do not desire, some to purchase desired services from a less efficient and more costly system, and others to forego services for which they would be willing to pay. These price differences most likely reflect differences in consumer demands for vehicle services and the costs of providing them efficiently. If price differences are no longer permitted fully to reflect the costs associated with

different distribution methods because of governmental intrusion into existing market mechanisms, then prices will rise to cover the higher-cost distribution methods. By negating existing efficiencies, these bills will raise the overall costs of the motor vehicle distribution system, thereby adversely affecting the interests of consumers.

An efficient distribution system enables both manufacturers and dealers to compete most effectively against their respective rivals and benefits consumers through the lowest possible prices. Because tailoring a distribution system to the diverse needs of different classes of customers can have these beneficial effects, multiple distribution systems frequently exist for other manufactured goods. For example, food, hardware, household goods, and other products are offered by large "no frills" stores, which may purchase directly from the manufacturer, as well as by small "mom and pop" stores that provide substantial services and which generally purchase through intermediaries. Similarly, products such as appliances and electronic and photographic equipment are distributed through service-oriented department stores, as well as through discount stores and mail-order catalog outlets that provide few, if any, services. By precluding manufacturers from charging different classes of purchasers different prices, H.R. 1415 and H.R. 5305 totally ignore the value of services provided and effectively would destroy the manufacturers' incentives and abilities to tailor different distributional

systems to different needs. Consumers thereby would be denied the benefits of the most efficient distribution system for motor vehicles.

II. The Bills Are Unnecessary

Proponents of H.R. 1415 and H.R. 5305 have labeled them as bills to prevent "unfair price discrimination." We are not aware that any price discrimination is occurring, and hence, we believe this characterization to be erroneous. Price discrimination occurs when prices charged do not reflect the costs of doing business with particular customers or groups of customers. Thus, price discrimination may occur when different prices are charged to persons for whom the cost of doing business is the same; conversely, it may occur when the same price is charged to persons for whom the costs of doing business are different. Because proponents of these bills have not shown that any differences in prices charged do not reflect the different costs of doing business with franchised dealers and high-volume purchasers, the existence of price discrimination has not been established. Even if there were some price differences not fully accountable by cost differences among different customer classes, these bills unnecessarily go far beyond existing prohibitions against price discrimination as prohibited by the Robinson-Patman Act, 15 U.S.C. § 13a et seq. Unlike that statute, H.R. 1415 and H.R. 5305 would prohibit essentially all price differences, even where no anticompetitive effect is observed and without

regard to other legitimate business justifications recognized by the Robinson-Patman Act, such as good faith meeting of competition or the reasonable availability of lower prices to other customers.

It has been argued by proponents of H.R. 1415 and H.R. 5305 that this legislation is necessary to prohibit manufacturers from "subsidizing" fleet sales. However, neither bill defines the term "subsidization" or contains any proposed Congressional findings as to precisely what conduct is alleged to be occurring. Accordingly, we are unaware of the specific basis upon which such a claim has been made. Moreover, any consideration of so-called "subsidization" requires careful identification and consideration of the common and overhead costs associated with producing vehicles for each group of purchasers, as well as the incremental or marginal costs of producing for each group. Without going into the technical complications, subsidization essentially requires that the group receiving the subsidy is paying less than the incremental cost of serving it, and that the group providing the subsidy is paying more than it would pay if the first group were not being served. Proponents of this legislation have not cited, nor are we aware of, any evidence that would tend to establish that any such conduct is occurring. Accordingly, the case for enactment of this legislation simply has not been made.

III. The Bills Will Lead To Inefficient Distribution And Higher Prices For Motor Vehicles

Rather than reflecting any so-called "subsidy" strategy, it is far more likely that any differences between prices charged high-volume purchasers and franchised dealers reflect differences in the relative costs of serving the different sets of customers. For example, scheduling production, credit, financing, delivery and road preparation services may be easier and less costly to provide to high-volume purchasers than to franchised dealers, thereby offering manufacturers scale and other economies in their sales to the former group. Second, recalls and other after-sale services requiring consumer notification are likely to be simpler and less costly with respect to high-volume purchasers. These factors can be expected to reduce manufacturers' costs of dealing with high-volume purchasers, thus enabling them to sell to such customers at prices lower than they must charge their other customers for whom such cost savings are not available.

Moreover, manufacturers' advertising expenditures intended to generate sales to individual consumers purchasing through franchised dealers should properly be attributed to vehicles sold through those dealers and not to vehicles whose sales are not affected by such advertising. Thus, proper allocation of advertising and other promotional services may also indicate that manufacturers' costs of dealing with high-volume purchasers are lower than their costs of dealing with

franchised dealers. These examples suggest the range of potential cost differences in serving the different sets of vehicle purchasers that are likely to account for any price differences that may exist. The ability to price in accordance with such differences is fully consistent with rational sales ~~(who could be expected to gain at the expense of consumers)~~ policies in a competitive environment, and benefits consumers by providing them the goods and services they desire at the lowest possible cost.

Our opposition to these bills is not mitigated by the exceptions they contain to the general rule that manufacturerers must charge the same prices for similar vehicles. That general rule will have serious adverse effects, which will not significantly be alleviated by the bills' narrow, limited and rigid exceptions. Rather, enactment of H.R. 1415 or H.R. 5305 would tend to rigidify manufacturer pricing decisions, and may also make it easier for manufacturers to collude on prices because price cutting to particular service outlets would be prohibited by law. Furthermore, since price differences among service outlets would not be permitted irrespective of the costs of providing motor vehicles to those outlets, in situations where the costs of supplying vehicles differ, competition among manufacturers must take the form of costly and inefficient service competition much like that observed in regulated industries

with fixed rates, such as experienced in the airline industry prior to deregulation.

I should also point out that enactment of H.R. 1415 or H.R. 5305 will undesirably increase litigation through creation of a new federal cause of action. Moreover, such litigation is likely to be expensive, time-consuming and complex due to the various possible standards for identifying vehicle models and their respective prices. In addition, manufacturerers faced with the requirements contained in these bills can be expected to seek to avoid their effects by further differentiating their models, particularly in light of the ease with which they could modify them by altering standard equipment or the options that are designated as standard. Such attempts will not only further increase the likelihood of litigation, but will also add to manufacturers' costs and make the bill largely unenforceable.

IV. Conclusion

Proponents of H.R. 1415 and H.R. 5305 have not shown that any price discrimination or "subsidization" of fleet purchasers is occurring, or that consumers are suffering any economic harm from the present method of sales to commercial and governmental high-volume purchasers. Rather, the dual distribution system employed by motor vehicle manufacturers appears to be efficient, to reflect the costs of dealing with different classes of customers, and to meet those customers' different needs at the lowest possible costs. Thus, to impose new, rigid regulations on manufacturers that would prohibit continuation

of existing pricing practices that are not alleged to be unlawful, as these bills would do, is against the public interest. The bills would destroy an efficient distribution system, increase costs to consumers and increase government regulation of private contracts in furtherance of the franchised dealers' special interest. For all these reasons, the Department of Justice strongly recommends against enactment of this legislation.

Mr. Chairman, that concludes my prepared remarks. I would be happy to respond to any questions that you or other members of the Committee may have.

T4-8/83.1 OMB

HR 5305

HR 1415

U.S. Department of Justice

Office of Legislative and Intergovernmental Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

08 JUN 1984

Honorable Peter W. Rodino, Jr.
Chairman
Committee on the Judiciary
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

This letter responds to your request for the views of the Department of Justice on H.R. 1415 and H.R. 5305, bills "to protect consumers and franchised automobile dealers from unfair price discrimination in the sale by the manufacturer of new motor vehicles." For the reasons set forth below, the Department of Justice strongly recommends against enactment of this legislation.

I. Description of the Bills and the Existing Motor Vehicle Distributional System

Although these bills are similar in that their essential feature is to prohibit price differentials to different classes of motor vehicle purchasers, they are different in certain respects. H.R. 1415 would substantially expand the "Automobile Dealers' Day in Court Act," 15 U.S.C. 1221 et seq., which governs certain relations between automobile manufacturers and their dealers. Section 1 (a) of H.R. 1415 provides that each franchise agreement between a motor vehicle dealer and manufacturer shall be deemed to prohibit the manufacturer from: (1) selling or offering to sell any vehicle to any person (including any other dealer) during any period of time at a price lower than that charged to its franchised dealers for the same, similarly equipped model during the same period of time; (2) imposing or enforcing any restriction on its dealers not imposed or enforced against any other purchaser; and (3) providing ultimate purchasers with any rebate, discount, refund, promotional service, additional equipment, or any other inducement or benefit not provided to all other ultimate purchasers of the same model during the same time period. An exception to prohibition (1) above permits the manufacturer to sell a vehicle to any person (including any other dealer) for resale to any unit of federal, state, or local government, but only if the manufacturer does not sell or offer to sell the same, similarly equipped model to any

other person for resale to any unit of government at any period of time at a price lower than that charged to the franchised dealer.

H.R. 5305, on the other hand, takes a somewhat different approach to achieve essentially the same result. Section 2 of that bill provides that no motor vehicle manufacturer may sell or lease any new vehicle to any person (including a dealer) during any sales period at a price higher than the lowest price at which any other vehicle of the same model, similarly equipped, is sold or leased, or offered for sale or lease, by the manufacturer during that sales period. Section 3 provides an exception allowing the manufacturer to sell or lease, or offer to sell or lease, any new vehicle to (1) a non-dealer employee of the manufacturer; (2) any department, agency, or instrumentality of the United States or of a State or local government; or (3) the American Red Cross. A further exemption in Section 3 permits the sale or offer to sell any new vehicle to any purchaser, if such sale or offer to sell by the manufacturer is part of a qualified regional incentive sales program for a designated region. To qualify, all vehicles of the same model, similarly equipped, sold or offered for sale by the manufacturer in the region during the period, must be sold and offered at the same price, and all vehicles sold in such region during such period must be delivered by the manufacturer to the purchaser in such regions.

Both bills would permit persons to bring actions against motor vehicle manufacturers for damages and injunctive relief based upon violations of the prohibitions contained in the respective bills. In addition, H.R. 5305 permits awards of punitive damages and attorneys fees in the discretion of the court.

Both bills would substantially alter motor vehicle manufacturers' existing relationships with their dealers and the present distribution system for such vehicles. As such, they appear to be based upon some belief that the existing distribution system for motor vehicles is not efficient and is flawed in ways that ultimately harm consumers. However, it is in the manufacturers' interest to choose the most efficient distribution system possible, so as to minimize the costs of distributing motor vehicles to ultimate consumers and thereby maximize their profits. Moreover, automobile manufacturers must compete among themselves for dealers and for sales to ultimate consumers. We are aware of no evidence that the existing distributional system is inefficient, nor are we aware of any reasons why manufacturers would choose an inefficient distribution system.

Currently, manufacturers distribute the great majority of their motor vehicles to franchised dealers, who provide particular services as desired by individual consumers and other low-volume purchasers. Manufacturers also distribute some of

their vehicles directly to high-volume purchasers, such as governmental units, taxi fleet operators, and rental car companies, who use those vehicles to provide products or services to consumers. Information we have seen indicates that, at present, high-volume sales account for only approximately 20% of the current motor vehicle market. The remaining 80% of such sales are made through franchised dealers.

Different groups of vehicle users value particular distribution services differently and are, therefore, willing to pay different amounts for those services. Thus, for example, an individual who desires to purchase an automobile for personal (or even business) use from a franchised dealer will demand a certain mix of services. Some of those services will be provided by the manufacturer (e.g., installation of certain options, warranty terms, and delivery to the dealer), while other services will be provided by the dealer (e.g., sales efforts, demonstrators, road preparation, and repair work under the warranty).

High-volume purchasers, on the other hand, may be willing to forego certain services or perform them themselves, saving manufacturers those costs and enabling manufacturers to charge such purchasers less than the price charged to franchised dealers. In addition, there may be some benefits to manufacturers as a result of use of their vehicles by high-volume purchasers that also benefit franchised dealers. For example, consumers get valuable information about the operation of vehicles they rent that may factor in their purchase decisions, and rental car company advertisements about the cars they lease likewise benefit both the manufacturers of those cars and their franchised dealers. If fleet car sales for some reason reduce the willingness of franchised dealers to provide services that most consumers want, then the manufacturer will lose sales and profits and, therefore, will have the incentive to restructure its fleet sales in a way that ensures that these services will be provided. The important point, however, is that through whatever channel the vehicles are distributed, consumers ultimately must bear the costs of the distribution system as purchasers of vehicles, as ultimate users of transportation services, and as taxpayers.

The ability of manufacturers to adjust their charges according to different services provided enables them to satisfy the varying demands of their different classes of purchasers at prices that reflect the costs of the services provided. If, as we believe, the existing system is efficient, then enactment of H.R. 1415 or H.R. 5305 may require some customers to pay for services they do not desire, some to purchase desired services from a less efficient and more costly system, and others to forego services for which they would be willing to pay. These price differences most likely reflect differences in consumer demands for vehicle services and the costs of providing them

efficiently. If price differences are no longer permitted fully to reflect the costs associated with different distribution methods because of governmental intrusion into existing market arrangements, then prices will rise to cover the higher-cost distribution methods. By negating existing efficiencies, these bills will raise the overall costs of the motor vehicle distribution system, thereby adversely affecting the interests of consumers.

An efficient distribution system enables both manufacturers and dealers to compete most effectively against their respective rivals and benefits consumers through the lowest possible prices. Because tailoring a distribution system to the diverse needs of different classes of customers can have these beneficial effects, multiple distribution systems frequently exist for other manufactured goods. For example, products such as appliances and electronic and photographic equipment are distributed through service-oriented department stores, as well as through discount stores and mail-order catalog outlets that provide few, if any, services. By precluding manufacturers from charging different classes of purchasers different prices, H.R. 1415 and H.R. 5305 totally ignore the value of services provided and effectively would destroy the manufacturers' incentives and abilities to tailor different distributional systems to different needs. Consumers thereby would be denied the benefits of the most efficient distribution system for motor vehicles.

II. The Bills Are Unnecessary

Proponents of H.R. 1415 and H.R. 5305 have labeled them as bills to prevent "unfair price discrimination." We are not aware that any price discrimination is occurring, and hence, we believe this characterization to be erroneous. Price discrimination occurs when prices charged do not reflect the costs of doing business with particular customers or groups of customers. Thus, price discrimination may occur when different prices are charged to persons for whom the cost of doing business is the same; conversely, it may occur when the same price is charged to persons for whom the costs of doing business are different. Because proponents of these bills have not shown that any differences in prices charged do not reflect the different costs of doing business with franchised dealers and high-volume purchasers, the existence of price discrimination has not been established. Even if there were some price differences not fully accountable by cost differences among different customer classes, these bills unnecessarily go far beyond existing prohibitions against price discrimination as prohibited by the Robinson-Patman Act, 15 U.S.C. § 13a et seq. Unlike that statute, H.R. 1415 and H.R. 5305 would prohibit essentially all price differences, even where no anticompetitive effect is observed and without regard to other legitimate business justifications recognized by the Robinson-Patman Act, such as good faith meeting of competition or the reasonable availability of lower prices to other customers.

It has been argued by proponents of H.R. 1415 and H.R. 5305 that this legislation is necessary to prohibit manufacturers from "subsidizing" fleet sales. However, neither bill defines the term "subsidization" or contains any proposed Congressional findings as to precisely what conduct is alleged to be occurring. Accordingly, we are unaware of the specific basis upon which such a claim has been made. Moreover, any consideration of so-called "subsidization" requires careful identification and consideration of the common and overhead costs associated with producing vehicles for each group of purchasers, as well as the incremental or marginal costs of producing for each group. Without going into the technical complications, subsidization essentially requires that the group receiving the subsidy is paying less than the incremental cost of serving it, and that the group providing the subsidy is paying more than it would pay if the first group were not being served. Proponents of this legislation have not cited, nor are we aware of, any evidence that would tend to establish that any such conduct is occurring. Accordingly, the case for enactment of this legislation simply has not been made.

III. The Bills Will Lead To Inefficient Distribution And Higher Prices For Motor Vehicles

Rather than reflecting any so-called "subsidy" strategy, it is far more likely that any differences between prices charged high-volume purchasers and franchised dealers reflect differences in the relative costs of serving the different sets of customers. For example, scheduling production, credit, financing, delivery and road preparation services may be easier and less costly to provide to high-volume purchasers than to franchised dealers, thereby offering manufacturers scale and other economies in their sales to the former group. Second, recalls and other after-sale services requiring consumer notification are likely to be simpler and less costly with respect to high-volume purchasers. These factors can be expected to reduce manufacturers' costs of dealing with high-volume purchasers, thus enabling them to sell to such customers at prices lower than they must charge their other customers for whom such cost savings are not available.

Moreover, manufacturers' advertising expenditures intended to generate sales to individual consumers purchasing through franchised dealers should properly be attributed to vehicles sold through those dealers and not to vehicles whose sales are not affected by such advertising. Thus, proper allocation of advertising and other promotional services may also indicate that manufacturers' costs of dealing with high-volume purchasers are lower than their costs of dealing with franchised dealers. These examples suggest the range of potential cost differences in serving the different sets of vehicle purchasers that are likely to account for any price differences that may exist. The ability

to price in accordance with such differences is fully consistent with rational sales policies in a competitive environment, and benefits consumers by providing them the goods and services they desire at the lowest possible cost.

Our opposition to these bills is not mitigated by the exceptions they contain to the general rule that manufacturers must charge the same prices for similar vehicles. That general rule will have serious adverse effects, which will not significantly be alleviated by the bills' narrow, limited and rigid exceptions. Rather, enactment of H.R. 1415 or H.R. 5305 would tend to freeze manufacturer pricing decisions and may also make it easier for manufacturers to collude on prices because price cutting to particular service outlets would be prohibited by law. Furthermore, since price differences among service outlets would not be permitted irrespective of the costs of providing motor vehicles to those outlets, in situations where the costs of supplying vehicles differ, competition among manufacturers must take the form of costly and inefficient service competition much like that observed in regulated industries with fixed rates, such as experienced in the airline industry prior to deregulation.

I should also point out that enactment of H.R. 1415 or H.R. 5305 will undesirably increase litigation through creation of a new federal cause of action. Moreover, such litigation is likely to be expensive, time-consuming and complex due to the various possible standards for identifying vehicle models and their respective prices. In addition, manufacturers faced with the requirements contained in these bills can be expected to seek to avoid their effects by further differentiating their models, particularly in light of the ease with which they could modify them by altering standard equipment or the options that are designated as standard. Such attempts will not only further increase the likelihood of litigation but will also add to manufacturers' costs and make the bill largely unenforceable.

IV. Conclusion

Proponents of H.R. 1415 and H.R. 5305 have not shown that any price discrimination or "subsidization" of fleet purchasers is occurring, or that consumers are suffering any economic harm from the present method of sales to commercial and governmental high-volume purchasers. Rather, the dual distribution system employed by motor vehicle manufacturers appears to be efficient, to reflect the costs of dealing with different classes of customers, and to meet those customers' different needs at the lowest possible costs. Thus, to impose new, rigid regulations on manufacturers that would prohibit continuation of existing pricing practices that are not alleged to be unlawful, as these bills would do, is against the public interest. The bills would destroy an efficient distribution system, increase costs to

consumers and increase government regulation of private contracts. For all these reasons, the Department of Justice strongly recommends against enactment of this legislation.

The Office of Management and Budget has advised this Department that there is no objection to the submission of this report from the standpoint of the Administration's Program.

Sincerely,

(Signed) Robert A. McConnell

Robert A. McConnell
Assistant Attorney General

HR 5305, (HR 1415) Final

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

JUL 17 1984

Honorable John D. Dingell
Chairman, Committee on Energy
and Commerce
U.S. House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

This is in response to your request for the views of the Department of Commerce concerning H.R. 5305, a bill

> "To protect consumers and franchised automobile dealers from unfair price discrimination in the sale by the manufacturer of new motor vehicles."

H.R. 5305 would prohibit an automobile manufacturer from selling or leasing any new automobile, or offering to sell or lease any new automobile, to any person (including an automobile dealer) at a price that is higher than the lowest price for which any other automobile of the same model is sold or offered during a particular sales period. The bill would provide exceptions for sales to employees of an automobile manufacturer, agencies of the United States or any state or local government, the American Red Cross, and sales under regional sales incentive programs. The prohibitions in the bill would be enforceable by private action.

The Department of Commerce opposes enactment of H.R. 5305. The legislation effectively would prohibit marketing practices that vehicle manufacturers and their fleet customers have found highly efficient and mutually beneficial. By requiring that the "lowest price" be the only selling price for a vehicle, H.R. 5305 would, despite its avowed intention to protect consumers and automobile dealers against "unfair price competition," be anti-competitive.

H.R. 5305 would eliminate or reduce competition in the fleet sales market by prohibiting large volume fleet purchase discounts. We believe that large volume fleet purchasers should be allowed to negotiate with manufacturers for lower prices. Fleet sales are an important factor in automobile manufacturing. Automobile companies can offer discounts on direct volume sales because such sales help reduce the per vehicle cost of manufacturing and thereby increase overall profits without raising prices to dealers. Fleet sales are often made in advance of initial vehicle production and thereby encourage the marketing of new products.

We have been advised by the Office of Management and Budget that there is no objection to the submission of this letter to the Congress from the standpoint of the Administration's position.

Sincerely,

Irving P. Margulies

Irving P. Margulies
General Counsel

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET

ROUTE SLIP

TO John Roberts	Take necessary action ☐
	Approval or signature ☐
	Comment ☐
	Prepare reply ☐
	Discuss with me ☐
	For your information ☐
	See remarks below ☐
FROM Branden Blum BB	**DATE** 9/17/84

REMARKS

H.R. 1415 and H.R. 5305, bills to protect consumers and franchised automobile dealers from unfair price discrimination in the sale by manufacturers of new motor vehicles

Per your request attched are copies of agency reports or testimony on the bills. I will forward to you upon receipt a copy of the signed Commerce report opposing S. 2770.

OMB FORM 4
Rev Aug 70

COMMISSION APPROVED

Statement of Barbara A. Clark

Deputy Director
Bureau of Competition
Federal Trade Commission

before the

Subcommittee on Commerce,
Transportation and Tourism
United States House of Representatives

June 7, 1984

Mr. Chairman, members of the subcommittee. Thank you for the opportunity to comment on H.R. 5305, a bill intended to protect consumers and franchised automobile dealers from unfair price discrimination in the sale of new motor vehicles by manufacturers. H.R. 5305 is a successor to H.R. 1415. While the bills address many of the same issues, H.R. 5305 is in part a reaction to Federal Trade Commission criticisms of H.R. 1415. While we appreciate the attempt to meet some of our concerns, we still have fundamental problems with the proposed legislation.

Essentially, H.R. 5305 requires a car manufacturer to sell (or lease) all similarly equipped cars of the same model to all direct purchasers, including dealers, at the same price. Where a manufacturer gives rebates or other benefits to indirect purchasers, the manufacturer's price to the direct purchasers generally cannot be higher than the effective price to the indirect purchasers.

I believe an analysis of the key provisions in H.R. 5305 reveals that this bill, like its predecessor, should not be enacted into law. In fact, this bill raises some legal problems

not present in the earlier bill in addition to the probable anticompetitive consequences we pointed out in our comments on H.R. 1415. I would like to briefly discuss our concerns with the specific sections of the bill.

Section 1: Definitions

A major definitional problem occurs in Section 1(5), which defines "sales period" as "any period of time during which a new automobile is sold or leased" at a specified price. This is the period to which the court would look to determine whether discriminatory prices are being offered in violation of Section 2. Section 1(5) may undermine the whole bill in large part because this section could be read to mean that the pertinent sales period ends as soon as a different price is instituted. Under this interpretation, a car manufacturer's new lower price to one purchaser could not violate Section 2, because the manufacturer's lower price institutes a new sale period, which terminates as soon as the manufacturer charges a new price to someone else. Although courts would try to interpret the law so that it would not be a nullity, they would have a difficult time determining what is meant by Section 1(5).

Section 1(6), with its broad "any . . . inducement or benefit" language, coupled with Section 2, presumably would end the manufacturers' present practice of delivering cars directly to large-volume purchasers. It would also presumably eliminate numerous other practices by which manufacturers presently

differentiate between consumers purchasing one car at a time and firms (such as automobile rental and leasing firms) purchasing thousands of cars each year. Thus, manufacturers would be inhibited from, for example, passing along savings in selling or delivery costs to large-volume purchasers.

Finally, Section 1(2) defines "automobile manufacturer" so broadly that it would potentially subject to liability companies totally unconnected to the manufacture of automobiles.

Section 2

Section 2, the heart of the bill, would outlaw price differences. Unlike the Robinson-Patman Act, this section does not allow for a cost-justification or meeting competition defense, typically used in price discrimination cases. There is no requirement that a dealer who pays a higher price than anyone else be injured by the price difference. In fact, there is no requirement that the dealer be in competition with the favored purchaser. Thus, a Hawaii dealer could win a price discrimination case because it paid a higher price for a certain car than a Michigan dealer located near the factory or than a Pennsylvania office supply firm purchasing cars for its salesmen.

Section 2 poses other problems. Couched in terms of "sell or lease," it could be read to prohibit a car manufacturer from selling a car to one person for a different price than the manufacturer's lease price to another person. In other words, the sales price and lease price of a particular type car may have

to be identical. This requirement could damage or end leasing programs that the public currently finds to be a worthwhile alternative to buying.

Section 3: Exceptions

Section 3 is an attempt to exempt sales at discriminatory prices to, among others, car factory workers, government agencies, and the American Red Cross. By restricting special treatment to these groups only, the bill would make it difficult for car manufacturers to modify their car distribution systems in the future to achieve more direct sales to non-dealers at competitive prices. Moreover, there is a non-profit institution exemption to the Robinson-Patman Act that is considerably broader than the exemption contained in H.R. 5305. There is no apparent reason for the Red Cross, as opposed to any other charitable organization, to be singled out for favorable treatment.

Section 4: Enforcement

Section 4, the enforcement section, could well subsidize barely-injured plaintiffs (and countless lawyers). Under this section, "[a]ny person may bring action . . . to require compliance" and seek punitive damages. The section does not require that the plaintiff be injured or that he even be a car purchaser. Section 4 goes considerably beyond the treble-damage remedy of the antitrust laws, since a plaintiff can recover the

amount of his injury many times over and plaintiffs need not even be injured, in an economic sense, to collect damages.

Under Section 4, if a manufacturer favored Hertz Corporation by giving it a $500 rebate on each of 60,000 cars purchased by Hertz, a dealer or other plaintiff could sue for punitive damages. The court would have discretion whether to grant the damages; however, if the court does decide in favor of damages, it "shall take into account" under Section 4(a)(3) the amount of the rebate times those 60,000 cars. Thus, injured (or uninjured) plaintiffs in the Hertz situation might be allowed to recover up to $30,000,000. Complications will inevitably result because the courts are given no direction on the limits of the damages that could be awarded or on proper damage apportionment. Any windfall damages defendant car manufacturers pay to uninjured plaintiffs may well be recouped at a later date through higher car prices to consumers.

Conclusion

The preceding analysis suggests a number of defects that make effective enforcement of H.R. 5305 problematic. In contrast to the proposed bill, the Robinson-Patman and Federal Trade Commission Acts are fully-formed statutes with established interpretations that are sufficient to handle the anticompetitive price discrimination problems this legislation is intended to address.

Even assuming that the bill's many serious interpretational problems are resolved, enactment of the bill may have anticompetitive consequences. For example, because the bill departs radically from traditional price discrimination law, lawful competitive price cuts and entry into new markets may be deterred. Manufacturers may fear testing the legal waters and may reasonably feel that the cost of litigation, even if successful, would be greater than the benefits of granting permissible discounts.

Next, discounts made to meet competition may help bring down high, "sticky" list prices in oligopolistic industries. A seller is particularly susceptible to hard bargaining from a variety of sources when the seller believes the buyer has gotten a special discount from one of the seller's competitors. Once price concessions are made, they will most likely become known throughout the industry and others will demand the same discount. Eventually, the high list price structure breaks down.

In addition, the bill may encourage the manufacture of automobiles that contain accessories not desired by consumers. The price discrimination prohibition in the act applies only to "similarly equipped" automobiles. A manufacturer wishing to evade the rigid confines of the act could market the most desirable autos to some buyers and then differentiate the product in some spurious way to other buyers. While product differentiation used as an evasion tactic is also possible under

the Robinson-Patman Act,[1] the bill under consideration leaves so little room for price differences (i.e., no cost justifications or meeting competition defenses are allowed) that manufacturers will be more likely to resort to devices to circumvent the law.

H.R. 5305, if enacted into law, can be expected to result in higher prices for consumers, price rigidity, or both. It would also inhibit car manufacturers from instituting pro-competitive and cost-justified changes in their pricing and car distribution systems. To the extent that price discrimination in automobile sales is causing significant competitive injury, the Robinson-Patman and Federal Trade Commission Acts provide better means for dealing with the problem.[2] Moreover, those Acts have well-known contours, whereas H.R. 5305 takes discrimination law into uncharted (and possibly dangerously anticompetitive) territory. The Commission therefore opposes enactment of this bill.

I will be happy to answer any questions you may have.

1/ That Act applies to the sale of commodities of like grade and quality.

2/ In response to an inquiry by Rep. Florio, the Chairman recently transmitted to the Bureau of Competition for further investigation and analysis allegations of unfair practices of a type that H.R. 5305 is intended to address.

SEPARATE STATEMENT OF COMMISSIONER PERTSCHUK CONCERNING H.R. 5305

June 6, 1984

I agree with most of the points made in the Commission's statement, but I wish to add two others. First, a significant issue relating to the need for H.R. 5305 is whether harmful price discrimination that is not technically prohibited by the Robinson-Patman Act can still be addressed under the FTC Act. I believe that the answer is certainly yes if the conduct falls within the standards of Grand Union Co. and related cases. 1/ Unfortunately, the majority declined to state this principle expressly in the testimony even though they were requested to do so. Consequently, the Committee may wish to question the Commission's representative on this point.

Second, the statement repeats the proposition included in the Commission's earlier letter to the Committee on H.R. 5305: "To the extent that price discrimination in automobile sales is causing competitive injury, the Robinson-Patman and Federal Trade Commission Acts provide better means for dealing with the problem." As I said in my separate statement accompanying that letter, this point only has meaning if the Robinson-Patman Act and analogous principles under the Federal Trade Commission Act are enforced. Not only has the current Commission failed to bring any new price discrimination cases during the entire period

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1/ Grand Union Co. v. FTC, 300 F.2d 92 (2d Cir. 1962).

of the administration, while nevertheless professing a commitment to enforcement in this area, the senior staff recently recommended closing two major investigations despite good indications that violations have occurred. In one case, the Bureau is apparently pursuing settlement negotiations, though the ultimate result is uncertain. In the other case, I moved in August 1983 to reject the Bureau's recommendation and to complete the investigation. Nevertheless the motion remains "on hold" because all Commissioners have still not voted.

Even more remarkably, perhaps, the current Commission periodically claims that Robinson-Patman Act enforcement has not diminished. 2/ While I admire the sheer exuberance of this denial of reality, the facts are that the only price discrimination orders issued by the Commission have been settlements of cases brought prior to this administration. Although the Chairman points frequently to the large number of investigations that are recorded as technically active on our computer lists, so far none of these investigations has resulted in an enforcement action.

2/ "[T]he Commission's current Robinson-Patman enforcement priorities are consistent with the trends and lessons of the last decade. . . . We definitely have not abandoned enforcement of the Robinson-Patman Act." Testimony of Chairman Miller to the Subcommittee on Commerce, Transportation and Tourism of the House Committee on Energy and Commerce, February 22, 1984, p. 5. "During the past four administrations, [Commissioner] Calvani observed, public sector Robinson-Patman Act enforcement has not changed appreciably." Antitrust and Trade Regulation Report, May 24, 1984, p. 1007.

Department of Justice

HR 1415
HR 5305
Final
Brauden

STATEMENT OF

CHARLES F. RULE
DEPUTY ASSISTANT ATTORNEY GENERAL
ANTITRUST DIVISION

BEFORE THE

SUBCOMMITTEE ON COMMERCE, TRANSPORTATION
AND TOURISM

COMMITTEE ON ENERGY AND COMMERCE

UNITED STATES HOUSE OF REPRESENTATIVES

CONCERNING

PRICE DIFFERENTIALS TO DIFFERENT CLASSES OF PURCHASERS
OF NEW MOTOR VEHICLES AND H.R. 1415 AND H.R. 5305,
BILLS "TO PROTECT CONSUMERS AND FRANCHISED
AUTOMOBILE DEALERS FROM UNFAIR PRICE DISCRIMINATION
IN THE SALE BY THE MANUFACTURER OF NEW MOTOR VEHICLES"

ON

JUNE 7, 1984

Mr. Chairman and Members of the Subcommittee:

I am pleased to have the opportunity to provide you with the views of the Department of Justice on H.R. 1415 and H.R. 5305, bills "to protect consumers and franchised automobile dealers from unfair price discrimination in the sale by the manufacturer of new motor vehicles." For the reasons I will discuss, the Department of Justice strongly recommends against enactment of this legislation.

I. Description of the Bills and the Existing Motor Vehicle Distributional System

Although these bills are similar in that their essential feature is to prohibit price differentials to different classes of motor vehicle purchasers, they are different in certain respects. H.R. 1415 would substantially expand the "Automobile Dealers' Day in Court Act," 15 U.S.C. 1221 et seq., which governs certain relations between automobile manufacturers and their dealers. Section 1 (a) of H.R. 1415 provides that each franchise agreement between a motor vehicle dealer and manufacturer shall be deemed to prohibit the manufacturer from: (1) selling or offering to sell any vehicle to any person (including any other dealer) during any period of time at a price lower than that charged to its franchised dealers for the same, similarly equipped model during the same period of time; (2) imposing or enforcing any restriction on its dealers not imposed or enforced against any other purchaser; and (3) providing ultimate

purchasers with any rebate, discount, refund, promotional service, additional equipment, or any other inducement or benefit not provided to all other ultimate purchasers of the same model during the same time period. An exception to prohibition (1) above permits the manufacturer to sell a vehicle to any person (including any other dealer) for resale to any unit of federal, state, or local government, but only if the manufacturer does not sell or offer to sell the same, similarly equipped model to any other person for resale to any unit of government at any period of time at a price lower than that charged to the franchised dealer.

H.R. 5305, on the other hand, takes a somewhat different approach to achieve essentially the same result. Section 2 of that bill provides that no motor vehicle manufacturer may sell or lease any new vehicle to any person (including a dealer) during any sales period at a price higher than the lowest price at which any other vehicle of the same model, similarly equipped, is sold or leased, or offered for sale or lease, by the manufacturer during that sales period. Section 3 provides an exception allowing the manufacturer to sell or lease, or offer to sell or lease, any new vehicle to (1) a non-dealer employee of the manufacturer; (2) any department, agency, or instrumentality of the United States or of a State or local government; or (3) the American Red Cross. A further exemption in Section 3 permits the sale or offer to sell any new vehicle to any purchaser, if such

sale or offer to sell by the manufacturer is part of a qualified regional incentive sales program for a designated region. To qualify, all vehicles of the same model, similarly equipped, sold or offered for sale by the manufacturer in the region during the period, must be sold and offered at the same price, and all vehicles sold in such region during such period must be delivered by the manufacturer to the purchaser in such regions.

Both bills would permit persons to bring actions against motor vehicle manufacturers for damages and injunctive relief based upon violations of the prohibitions contained in the respective bills. In addition, H.R. 5305 permits awards of punitive damages and attorneys fees in the discretion of the court.

Both bills would substantially alter motor vehicle manufacturers' existing relationships with their dealers and the present distribution system for such vehicles. As such, they appear to be based upon some belief that the existing distribution system for motor vehicles is not efficient and is flawed in ways that ultimately harm consumers. However, it is in the manufacturers' interest to choose the most efficient distribution system possible, so as to minimize the costs of distributing motor vehicles to ultimate consumers and thereby maximize their profits. Moreover, automobile manufacturers must compete among themselves for dealers and for sales to ultimate consumers. We are aware of no evidence that the existing distributional system is inefficient, nor are we aware of any reasons why manufacturers would choose an inefficient distribution system.

Currently, manufacturers distribute the great majority of their motor vehicles to franchised dealers, who provide particular services as desired by individual consumers and other low-volume purchasers. Manufacturers also distribute some of their vehicles directly to high-volume purchasers, such as governmental units, taxi fleet operators, and rental car companies, who use those vehicles to provide products or services to consumers. Information we have seen indicates that, at present, high-volume sales account for only approximately 20% of the current motor vehicle market. The remaining 80% of such sales are made through franchised dealers.

Different groups of vehicle users value particular distribution services differently and are, therefore, willing to pay different amounts for those services. Thus, for example, an individual who desires to purchase an automobile for personal (or even business) use from a franchised dealer will demand a certain mix of services. Some of those services will be provided by the manufacturer (e.g., installation of certain options, warranty terms, and delivery to the dealer), while other services will be provided by the dealer (e.g., sales efforts, demonstrators, road preparation, and repair work under the warranty).

High-volume purchasers, on the other hand, may be willing to forego certain services or perform them themselves, saving manufacturers those costs and enabling manufacturers to charge

such purchasers less than the price charged to franchised dealers. In addition, there may be some benefits to manufacturers as a result of use of their vehicles by high-volume purchasers that also benefit franchised dealers. For example, consumers get valuable information about the operation of vehicles they rent that may factor in their purchase decisions, and rental car company advertisements about the cars they lease likewise benefit both the manufacturers of those cars and their franchised dealers. If fleet car sales for some reason reduce the willingness of franchised dealers to provide services that most consumers want, then the manufacturer will lose sales and profits and, therefore, will have the incentive to restructure its fleet sales in a way that ensures that these services will be provided. The important point, however, is that through whatever channel the vehicles are distributed, consumers ultimately must bear the costs of the distribution system as purchasers of vehicles, as ultimate users of transportation services, and as taxpayers.

The ability of manufacturers to adjust their charges according to different services provided enables them to satisfy the varying demands of their different classes of purchasers at prices that reflect the costs of the services provided. If, as we believe, the existing system is efficient, then enactment of H.R. 1415 or H.R. 5305 may require some customers to pay for services they do not desire, some to

purchase desired services from a less efficient and more costly system, and others to forego services for which they would be willing to pay. These price differences most likely reflect differences in consumer demands for vehicle services and the costs of providing them efficiently. If price differences are no longer permitted fully to reflect the costs associated with different distribution methods because of governmental intrusion into existing market arrangements, then prices will rise to cover the higher-cost distribution methods. By negating existing efficiencies, these bills will raise the overall costs of the motor vehicle distribution system, thereby adversely affecting the interests of consumers.

An efficient distribution system enables both manufacturers and dealers to compete most effectively against their respective rivals and benefits consumers through the lowest possible prices. Because tailoring a distribution system to the diverse needs of different classes of customers can have these beneficial effects, multiple distribution systems frequently exist for other manufactured goods. For example, products such as appliances and electronic and photographic equipment are distributed through service-oriented department stores, as well as through discount stores and mail-order catalog outlets that provide few, if any, services. By precluding manufacturers from charging different classes of purchasers different prices, H.R. 1415 and H.R. 5305 totally

ignore the value of services provided and effectively would destroy the manufacturers' incentives and abilities to tailor different distributional systems to different needs. Consumers thereby would be denied the benefits of the most efficient distribution system for motor vehicles.

II. The Bills Are Unnecessary

Proponents of H.R. 1415 and H.R. 5305 have labeled them as bills to prevent "unfair price discrimination." We are not aware that any price discrimination is occurring, and hence, we believe this characterization to be erroneous. Price discrimination occurs when prices charged do not reflect the costs of doing business with particular customers or groups of customers. Thus, price discrimination may occur when different prices are charged to persons for whom the cost of doing business is the same; conversely, it may occur when the same price is charged to persons for whom the costs of doing business are different. Because proponents of these bills have not shown that any differences in prices charged do not reflect the different costs of doing business with franchised dealers and high-volume purchasers, the existence of price discrimination has not been established. Even if there were some price differences not fully accountable by cost differences among different customer classes, these bills unnecessarily go far beyond existing prohibitions against price

discrimination as prohibited by the Robinson-Patman Act, 15 U.S.C. § 13a et seq. Unlike that statute, H.R. 1415 and H.R. 5305 would prohibit essentially all price differences, even where no anticompetitive effect is observed and without regard to other legitimate business justifications recognized by the Robinson-Patman Act, such as good faith meeting of competition or the reasonable availability of lower prices to other customers.

It has been argued by proponents of H.R. 1415 and H.R. 5305 that this legislation is necessary to prohibit manufacturers from "subsidizing" fleet sales. However, neither bill defines the term "subsidization" or contains any proposed Congressional findings as to precisely what conduct is alleged to be occurring. Accordingly, we are unaware of the specific basis upon which such a claim has been made. Moreover, any consideration of so-called "subsidization" requires careful identification and consideration of the common and overhead costs associated with producing vehicles for each group of purchasers, as well as the incremental or marginal costs of producing for each group. Without going into the technical complications, subsidization essentially requires that the group receiving the subsidy is paying less than the incremental cost of serving it, and that the group providing the subsidy is paying more than it would pay if the first group were not being served. Proponents of this legislation have not cited, nor are we aware of, any evidence that would tend to establish that any such conduct is occurring. Accordingly, the case for enactment of this legislation simply has not been made.

III. The Bills Will Lead To Inefficient Distribution And Higher Prices For Motor Vehicles

Rather than reflecting any so-called "subsidy" strategy, it is far more likely that any differences between prices charged high-volume purchasers and franchised dealers reflect differences in the relative costs of serving the different sets of customers. For example, scheduling production, credit, financing, delivery and road preparation services may be easier and less costly to provide to high-volume purchasers than to franchised dealers, thereby offering manufacturers scale and other economies in their sales to the former group. Second, recalls and other after-sale services requiring consumer notification are likely to be simpler and less costly with respect to high-volume purchasers. These factors can be expected to reduce manufacturers' costs of dealing with high-volume purchasers, thus enabling them to sell to such customers at prices lower than they must charge their other customers for whom such cost savings are not available.

Moreover, manufacturers' advertising expenditures intended to generate sales to individual consumers purchasing through franchised dealers should properly be attributed to vehicles sold through those dealers and not to vehicles whose sales are not affected by such advertising. Thus, proper allocation of advertising and other promotional services may also indicate that manufacturers' costs of dealing with high-volume purchasers are lower than their costs of dealing with franchised dealers. These examples suggest the range of potential cost differences in

serving the different sets of vehicle purchasers that are likely to account for any price differences that may exist. The ability to price in accordance with such differences is fully consistent with rational sales policies in a competitive environment, and benefits consumers by providing them the goods and services they desire at the lowest possible cost.

Our opposition to these bills is not mitigated by the exceptions they contain to the general rule that manufacturers must charge the same prices for similar vehicles. That general rule will have serious adverse effects, which will not significantly be alleviated by the bills' narrow, limited and rigid exceptions. Rather, enactment of H.R. 1415 or H.R. 5305 would tend to freeze manufacturer pricing decisions and may also make it easier for manufacturers to collude on prices because price cutting to particular service outlets would be prohibited by law. Furthermore, since price differences among service outlets would not be permitted irrespective of the costs of providing motor vehicles to those outlets, in situations where the costs of supplying vehicles differ, competition among manufacturers must take the form of costly and inefficient service competition much like that observed in regulated industries with fixed rates, such as experienced in the airline industry prior to deregulation.

I should also point out that enactment of H.R. 1415 or H.R. 5305 will undesirably increase litigation through creation of a new federal cause of action. Moreover, such litigation is

likely to be expensive, time-consuming and complex due to the various possible standards for identifying vehicle models and their respective prices. In addition, manufacturers faced with the requirements contained in these bills can be expected to seek to avoid their effects by further differentiating their models, particularly in light of the ease with which they could modify them by altering standard equipment or the options that are designated as standard. Such attempts will not only further increase the likelihood of litigation but will also add to manufacturers' costs and make the bill largely unenforceable.

IV. Conclusion

Proponents of H.R. 1415 and H.R. 5305 have not shown that any price discrimination or "subsidization" of fleet purchasers is occurring, or that consumers are suffering any economic harm from the present method of sales to commercial and governmental high-volume purchasers. Rather, the dual distribution system employed by motor vehicle manufacturers appears to be efficient, to reflect the costs of dealing with different classes of customers, and to meet those customers' different needs at the lowest possible costs. Thus, to impose new, rigid regulations on manufacturers that would prohibit continuation of existing pricing practices that are not alleged to be unlawful, as these bills would do, is against the public interest. The bills would destroy an efficient distribution system, increase costs to consumers and increase government regulation of private contracts. For all

increase government regulation of private contracts. For all these reasons, the Department of Justice strongly recommends against enactment of this legislation.

Mr. Chairman, that concludes my prepared remarks. I would be happy to respond to any questions that you or other members of the Subcommittee may have.

DOJ-1984-06

Washington, D.C. 20230

JAN 10 1984

Honorable James J. Florio
Chairman, Subcommittee on Commerce,
Transportation and Tourism
Committee on Energy and Commerce
U.S. House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

The Department of Commerce has reviewed H.R. 1415, a bill

> "To protect franchised automobile dealers from unfair price discrimination in the sale by the manufacturer or importer of new motor vehicles,"

and we hereby submit our views on the legislation.

Under H.R. 1415, an automobile manufacturer would be prohibited from (a) selling or leasing any passenger car, truck or station wagon to any person at a price lower than that accorded to its franchised dealers; (b) imposing upon a dealer any restrictions that are not imposed upon all other purchasers; and (c) providing to a purchaser any rebate or discount that is not provided to all purchasers. In addition, a manufacturer would be unable to sell a vehicle to any person for resale to a unit of federal, state or local government at a price which is lower than the price at which the vehicle is sold to a dealer during the same period for resale to a unit of government.

We oppose enactment of H.R. 1415. Despite its avowed intention to provide protection against "unfair price discrimination," in reality the bill would prohibit marketing practices that vehicle manufacturers and their fleet customers have found highly efficient and mutually beneficial. We believe H.R. 1415 is anti-competitive and designed to benefit the special interests of franchised automobile dealers at the expense of American consumers.

H.R. 1415 would eliminate competition in the fleet sales market by prohibiting large volume fleet purchasers, including the federal government, from negotiating with automobile manufacturers for lower prices. We believe that large volume fleet purchasers,

Prepared by: OAGC/L Lisa Lindeman 377-1328

bcc: EA (C. Miller)
IPM Chron
GC Chron
File H.R. 1415
Lisa Lindeman

Office of Management and Budget

including the federal government, should be allowed to negotiate with manufacturers for lower prices in order to enhance competition and encourage efficient allocation of resources.

We understand that the Department of Justice is opposed to the bill because it would prohibit discounts on direct sales by manufacturers both to governmental and commercial fleet purchasers, and that the Department intends to submit a report outlining its opposition to the bill which will focus on its undesirable effects.

We have been advised by the Office of Management and Budget that there is no objection to the submission of this letter to the Congress from the standpoint of the Administration's position.

Sincerely,

Irving P. Margulies
Acting General Counsel